SUBMISSION TO THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

by

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INTRODUCTION

I would like to thank the committee for the opportunity to present the Government of British Columbia's views on the federal government's proposed Goods and Services Tax (GST).

I recognize that it is somewhat unusual for a provincial cabinet minister to appear in this forum. However, I want to point out that the proposed introduction of the GST is but a symptom of a much more serious problem facing this country today. I am concerned. The western premiers and their finance ministers are all concerned. So, I am committed to take whatever steps are necessary to make our concerns known.

The Government of British Columbia has opposed the replacement of the existing federal sales tax with a federal-only value added tax. We opposed it when the federal government first floated the idea as a trial balloon in 1985 and we have opposed the GST since it was announced in the 1989 federal budget. In November, 1989 I met with Donald Blenkarn, Chairman of the House of Commons Standing Committee on Finance, to voice our opposition.

More recently the British Columbia legislature passed a unanimous resolution condemning the GST and urging the federal government to withdraw the proposed new tax.

We believe that the GST is seriously flawed, but more importantly, the whole rationale for imposing a federal retail tax is flawed when we review our current fiscal situation.

It is no secret that the federal government sees the GST as a solution to its current budgetary crisis, an attempt to stem the red ink and slow the growth of the mountain of debt. I am told that if the $350 billion federal debt was translated into $100 bills we could paper the Trans-Canada highway from here (Vancouver) to Toronto.

Indeed, as a nation, we are in dire straits financially. But, as the finance minister of a province which has balanced its budget and reduced our debt, I am

frustrated by the federal mindset that sees a tax grab as the only solution to our fiscal dilemma. There is another option, and that is to cut expenditures. It is not the time to go to the people for more money, but to get our house in order, and reduce the debt by managing expenditures more effectively.

I would like to speak to you today about the root causes of the current fiscal trauma we are experiencing, and about alternatives to the GST. But first, let me clarify why British Columbia is opposed to this tax.

THE GOODS AND SERVICES TAX - A FLAWED TAX

Everyone agrees that the existing 13.5 per cent federal sales tax (FST) is flawed, although I must add that these flaws were far less important in 1984 when the tax rate was only nine per cent.

Unfortunately, the GST "cure" is worse than the FST "disease."

The most obvious flaw of the GST is that it is extremely complex. It will make Canada the first developed country to impose two distinct levels of retail sales tax. Retailers, whose jobs are not easy at the best of times, will suddenly be faced with problems of whether an item is taxable federally, taxable provincially, neither, or both. And the so-called simplified accounting methods that will be used to deal with this problem are not as straightforward as has been claimed.

Ironically, it is the small to medium sized businesses who will be hardest hit by the complexity of the GST. Given that this sector is a key to job creation and economic health, we should be extremely chary of adding to their administrative burden.

It is hardly surprising that the small business community has been a particularly vocal critic of the GST.

Central Canada is already moving into a recession. The GST threatens British Columbia's, and indeed Canada's, fragile economic health. By the federal government's own estimates, the introduction of the GST will add one and a

quarter per cent to price levels. And this is an optimistic estimate based on businesses passing on savings from the removal of the FST. The inflationary effect could well be much worse. It will represent a significant price shock to the economy - at a time when high interest rates and an artificially high dollar are already choking off economic growth.

The western premiers recently expressed their concerns about the effect of the federal government's high interest rate policy on the export-dependent economies of the western provinces.

The GST will fuel inflation, pushing up interest rates. Continued high interest rates relative to those in the United States will keep the value of the Canadian dollar artificially high and make British Columbia's exports less competitive in world markets. Why would we tempt fate at this time of economic uncertainty?

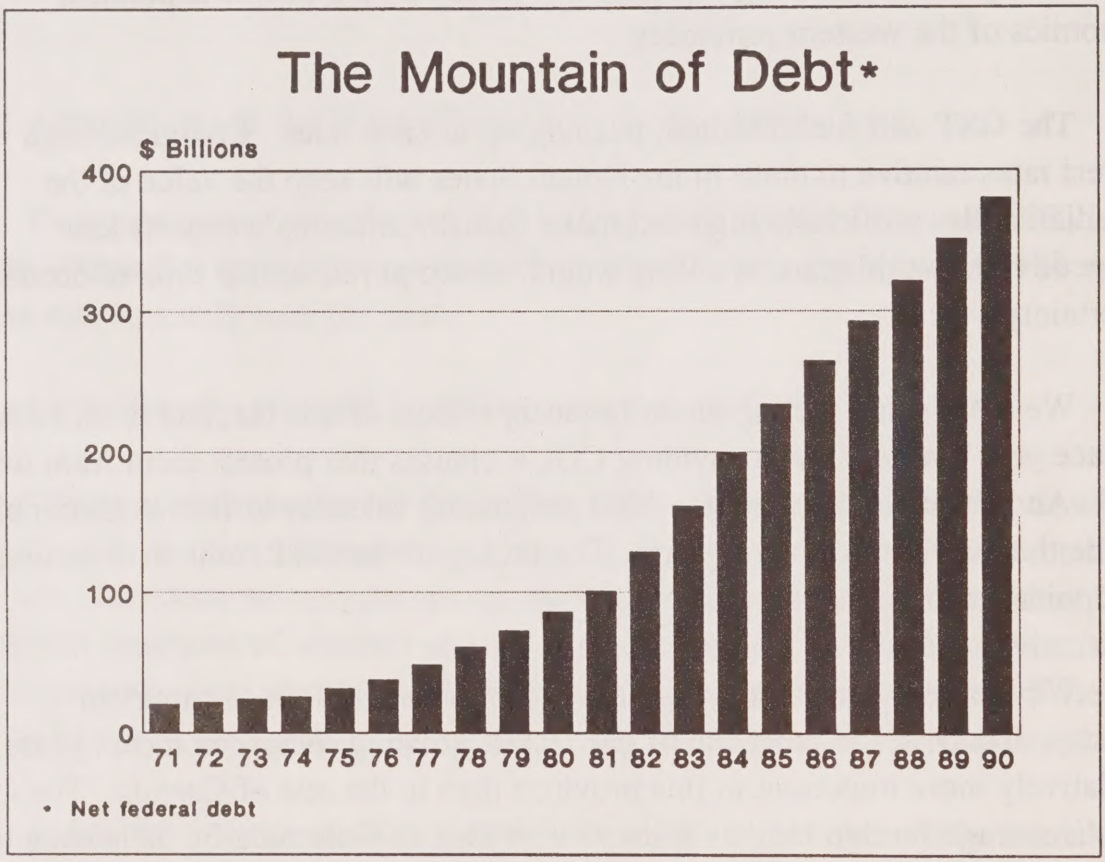
We are already feeling the inflationary effects of this tax, and it isn't even in place yet! Workers are demanding COLA clauses that protect them from the GST. And, I should note that the 1991 bargaining calendar in British Columbia will be the heaviest in several years. The timing of the GST from an economic standpoint could not be worse.

We are very concerned about the effect of the GST on our tourism industry. Tourism has been one of our fastest growing sectors in recent years. It is relatively more important in this province than in the rest of Canada. The GST will discourage foreign tourists from visiting British Columbia by increasing the cost of meals and entertainment, but it will also encourage Canadians to vacation abroad where services and accommodation will be easier on the pocketbook.

To summarize, British Columbia opposes the GST because it will complicate life for individuals and businesses, and because it threatens the competitiveness of our key industries. The GST is a revenue grab, pure and simple. It is a desperate, unimaginative attempt by the federal government to maintain the status quo so it can continue to live beyond its means.

THE GST: A SYMPTOM OF FAILED FISCAL MANAGEMENT

Earlier I called the GST a symptom of a far more serious problem. That problem is the federal government's inability or unwillingness to recognize the urgent need to deal with the critical economic and fiscal issues facing the country. The most important factor affecting the country's economic prospects is the rapidly growing mountain of federal debt.



The federal budget has been, and continues to be, held hostage to the public debt. Because of the large federal debt, interest costs are absorbing over 35 cents of every dollar the government takes in. Taxpayers are receiving only 65 cents worth of services for every dollar of tax they pay.

Contrast this with how we have managed our finances in British Columbia. Here, taxpayers receive 96 cents worth of services for every dollar of tax they pay.

Today, the federal budget deficit relative to the size of the Canadian economy is among the highest of all major industrialized countries, second only to Italy.

Even with this dismal record, the federal government is still spending way beyond its means. This fiscal year, the deficit is projected to total $28.5 billion. The government expects to spend $41.2 billion in interest alone. Let's put this in perspective—each Canadian taxpayer is paying over $3,000 just for interest alone. And, the $41.2 billion that Ottawa will pay in interest is more than the combined budgets of British Columbia, Alberta and Saskatchewan.

Canadian householders know that they can't spend more than they earn without eventually getting into serious difficulty. Yet, the federal government continues to do so.

With interest costs rising so rapidly and absorbing such a large part of the federal budget, the first priority of government must be to put the national fiscal house in order. The answer is not the GST quick fix. The answer is to balance the budget over the medium term by **setting spending priorities,** while recognizing revenue constraints.

THE OTHER "SOLUTION" TO THE DEFICIT PROBLEM: FEDERAL OFFLOADING

We want the federal government to reduce its deficit—the country's future depends on it. However, this should not be done through a revenue grab or by shifting the deficit to the provinces.

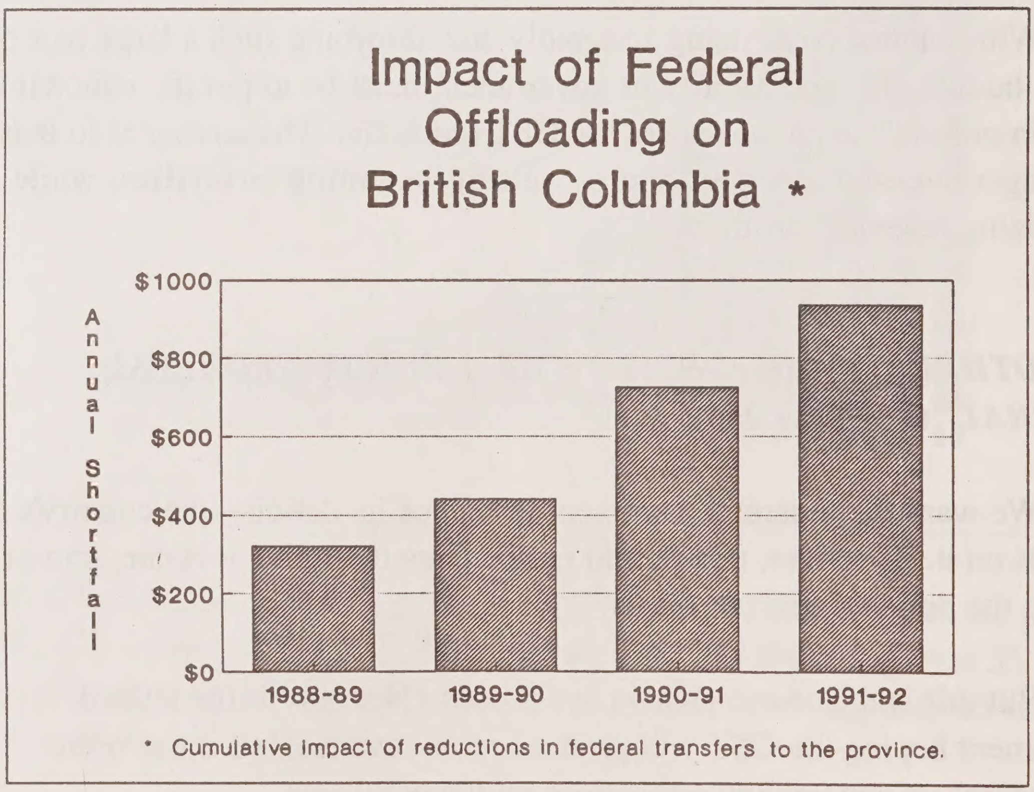
But this is the course Ottawa has chosen. Not only is the federal government hoping the GST will produce more revenue, but it has been "offloading" its expenditure obligations on the provinces.

Much of the success the federal government has shown in program restraint has been at the expense of the provinces. A considerable portion of budget savings in recent years have been realized by reducing the planned

transfer payments to the provinces, particularly the Established Programs Financing (EPF) transfers for post-secondary education and health care. Actions taken in the 1990 federal budget to freeze EPF transfers will cost British Columbia over $900 million over the next five years. The cumulative effect of this and other reductions in federal transfers amounts to more than $700 million in the current fiscal year alone.

Even if the federal government was able to get rid of all transfer payments to the provinces, it would still show a $5 billion deficit this year. This is clear evidence that offloading is not a viable strategy for eliminating the deficit.

At the same time as the federal government is reducing its commitment to programs it had a key role in starting, it continues to insist that provinces adhere to national standards.



The provinces are being put in a vise. We are being squeezed on the revenue side by the GST's intrusion into our tax field, and on the expenditure side by the offloading of program costs. Federal program standards are also limiting our freedom to manage our own expenditures.

British Columbia says “no more.” Saying no to the GST means saying no to more federal spending on new programs—new programs we can't afford with a federal debt equal to almost $15,000 for every man, woman and child in the country.

It is time to seek more fundamental solutions.

THE PRESENT STYLE OF FEDERALISM LEADS TO MORE SPENDING

What is a fundamental solution? Let’s revisit these arrangements. Let’s fix this overlap between the federal government and the provinces. Let’s devise a system where it becomes clear who is accountable.

For too many years, the federal government has cajoled and bribed its way into areas of provincial jurisdiction. The provinces have been lured into the trap of shared-cost programs by a federal government currying favour with its voters and special interests. This has created demands for services we can't afford to provide. The federal government enticed the provinces to provide most of our major social programs by offering to share eligible costs on a 50:50 basis. Thus evolved the Canadian phenomenon of "50-cent dollars": the provinces received $1 worth of benefits for every 50 cents they spent in these areas.

Recognizing that program costs were growing far faster than had been expected, the federal government began to withdraw from cost-sharing in the 1970s.

The current offloading strategy is the unfortunate result of the last twenty or thirty years of the “big government” agenda of successive federal governments. This agenda created unaffordable public demand for all kinds of services. Ottawa then backed away, in effect leaving provinces holding the bag.

One would think that facing a rising deficit in the 1980s would have limited the federal government's interest in new programs. Instead, several initiatives in areas of provincial jurisdiction were announced:

- the federal government's strategy to replace existing day care funding through the Canada Assistance Plan with a new scheme promising much more comprehensive coverage;

- the Prime Minister's promotion of a national education strategy, intended to improve the teaching of science-related subjects in school;

- attempts to capture the environmental agenda by pre-empting provincial regulatory authority;

- the institution of a federal Department of Forestry even though the federal government has no actual forest management responsibility;

- the recently-announced $300-million program to reduce high school dropout rates; this is an area of **exclusive** provincial jurisdiction; and

- the federal *Young Offenders Act*, which placed many expenditure obligations on provincial governments.

So even as the deficit proves increasingly difficult to control, the federal government continues to develop new programs and otherwise involve itself in areas of provincial jurisdiction. In many cases, these are areas where Ottawa has no experience, no program infrastructure and no responsibility. What are the consequences?

- waste, duplication and overlap;

- no one level of government is accountable to the taxpayer; and

- the federal government increases demand for provincial programs without being responsible for raising the revenues to pay for them, and no

one monitors the effectiveness of these programs or questions whether they are still relevant.

As a result, a permanent upward bias in spending threatens the fiscal stability of both levels of government.

TOWARD A SOLUTION: RE-FINANCING CONFEDERATION

The traditional federal approach to addressing its deficit - cutting transfer payments - merely shifts the federal deficit problem to the provinces. Neither is the solution to develop new taxes like the GST; these only whet government's appetite to spend.

A better way must be found to manage and control public finances in Canada. It is unacceptable to continue what has been occurring in our country. Any new fiscal arrangements must contribute to nation-building, rather than being a source of discord and disunity.

British Columbia proposes a new relationship between the provinces and the federal government, a relationship that parallels the emerging worldwide search for more local autonomy, evidenced in the Soviet Union, Great Britain, and elsewhere in Europe.

This new relationship would accept the principle of equalization to support the "have not" provinces as one of the central pillars of Confederation.

This proposed program for national renewal is designed to:

1) **Bring government closer to the people by:**

- discussion, consultation and public participation through national referenda on major issues; and

- returning control of “people” programs to the provinces, who have a better understanding of the needs of their citizens.

2) **Give provinces greater freedom to carry out their responsibilities by:**

- more clearly defining federal and provincial areas of jurisdiction;

- better matching revenues with constitutional responsibility for major social programs through transfers of tax points from the federal government to the provinces;

- permitting provinces to design their own tax systems within the existing Tax Collection Agreement, recognizing that a lack of flexibility will lead to provincial withdrawal from this agreement; and

- allowing provinces to work together to remove the strait-jacket of federally-imposed standards which are no longer affordable.

3) **Involve provinces in decisions that affect them through:**

- reform of federal institutions such as the Bank of Canada and regulatory agencies to provide for shared decision-making rather than just consultation; and

- co-operation in areas of national interest such as transportation, communications, international trade and economic policy; this would recognize the inexorable march toward globalization.

4) **Regain fiscal control:**

Strong, broad-based political will to restore fiscal integrity must be found by:

- all levels of government working cooperatively to dampen public demands for new programs, and removing standards that prevent effective cost control; and

- a federal challenge to the provinces to legislate limits on their taxation and spending and an agreement to put savings from improved fiscal control toward national debt reduction.

The new relationship between the federal government and the provinces would bring government closer to the people. It would resolve the ambiguous and expensive system of divided management responsibility for programming. It would provide for shared decision-making in areas affecting provinces and their citizens.

To begin the process of renewing our federation, western premiers last week called for a meeting of federal and provincial finance ministers and treasurers to deal with the nation's finances.

CONCLUSION

The federal government's Goods and Services Tax is a symptom of a fundamental problem with the management of public finances in this country—it is not a solution.

The Government of British Columbia believes that only through a fundamental re-ordering and re-definition of the roles and responsibilities of the federal and provincial governments can we begin to chip away at the mountain of public sector debt and work toward national renewal.

The time to act is now.

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